


Non-Executive Report of the: PENSIONS BOARD 31st July 2017	
Report of: Zena Cooke, Corporate Director of Resources	Classification:
Future Options for Pension Administration Services	

Originating Officer(s)	George Bruce, Interim Pensions Manager
Wards affected	All

Introduction:

Pension Administration services to the Tower Hamlets Pension Scheme are provided by the Council's in-house Pensions Team. This paper identifies alternative arrangements for providing an administration service, considers the advantages and challenges of the current arrangements and compares these with alternative arrangements. The paper concludes that further investigation should be undertaken of the alternatives discussed in the paper to be followed by a recommendation to the next Committee meeting.

The options being discussed do not involve the pension investment and finance teams. It is recommended that further detailed evaluation of the options outlined in the paper, including discussion with other local authorities, is undertaken.

Recommendations:

The Pensions Board is recommended to consider and comment on the contents of the report.

1. REASONS FOR THE DECISIONS

1.1 The LGPS is becoming increasing complex due to the frequent changes in legislation, regulation and best practice guidance. It is also under greater scrutiny through the enhanced role given to the Pensions Regulator. Maintaining awareness of and implementing new regulations is a challenge for a small team. Additionally, a small team such as that which operates in Tower Hamlets faces inherent risks from losing key staff. Working as part of a multi-client grouping will enable the resources required to demonstrate compliance with best practice to be shared and potentially offer greater resilience and transparency of performance.

2. ALTERNATIVE OPTIONS

2.1 The report fully explores the available options.

3. DETAILS OF REPORT

Introduction

- 3.1 Services to the Pension Scheme are delivered by the Council's HR and Finance Departments. Finance provides investment and accounting support, while the Pensions team in HR maintain the records of contributing members, calculate and pay benefits and deal with employer issues. This report is concerned solely with the HR aspects of pension support.
- 3.2 The Pensions team comprises seven people. There are currently eight staff including three interims and one apprentice reflecting a need to replace three retired, seconded and maternity leave staff and to progress ongoing projects. Recent reviews by the LGA and Internal Audit have indicated procedural weaknesses in the team in the prolonged absence of the Pensions Manager. Although these issues are being addressed they indicate the vulnerability of small specialist teams to the loss of key staff.
- 3.3 The current in-house pension team has been in place at least 30 years and probably since the establishment of LB Tower Hamlets. Most London Boroughs have historically relied upon in-house pension administration, although this has been changing in recent years and now only 12 of the 32 London Boroughs have single borough in-house pension teams. Appendix A lists the pension arrangements for all London Boroughs.
- 3.4 This report will firstly look at the advantages and challenges of running a single borough in-house pension team. Alternative arrangements will be outlined and although a recommendation is made to investigate the option of working collaboratively with other Local Authorities there is no proposal at this stage to alter the existing arrangements. Following the Committee meeting, detailed evaluation of the alternatives outlined in the paper will be undertaken before the September meeting.

Advantages and drawbacks of the current arrangements

- 3.5 In comparing an in-house team with other possible structures there are both strengths and challenges to retaining an in-house team. These are explored below. Some of the challenges can be addressed, although residual risk may always remain as explained below.

Advantages of an in-house team

Direct control over the quality of the service.

With an in-house team, management are in full control and can alter the priorities, the targets, the resources and procedures / processes. Working with others involves a degree of loss of control.

Direct relationship with scheme members and other third parties

Currently, communication and service to scheme members is direct and not via an intermediary. Similar, there is direct contact with all service suppliers e.g. actuary.

Avoidance of conflicts from the needs of other clients

The in-house team only has one client and is therefore free from having to structure a service to balance the needs of multiple clients.

Certainty for staff

Continuing the current arrangements offers continuity for current staff.

- 3.6 Alongside the advantages of the current in-house arrangement there are a number of challenges. Calling these challenges reflects that many can be mitigated but that risks remain. These are:

Reliance of a few skilled staff

Small teams are inherently reliant on a few skilled individuals, with knowledge of key processes often known to only one or two. Staff changes can therefore have a significant impact on service levels.

Increasing complexity and regulatory oversight

The LGPS and pensions generally are increasingly complex and subject to regulatory oversight. Maintaining awareness of responsibilities and delivering a high quality service at a reasonable cost is challenging for a small team in such an evolving and complex environment. Regulatory oversight means that doing things well is only part of the requirement. There is also a need to demonstrate that compliance has been achieved.

Focus tends to be on day-to-day workload

Projects that are time consuming to implement but lead to efficiency savings can be difficult to progress when resourced from the existing team.

Higher costs

Costs, in particular project and IT, can be high for small schemes measured on a cost per member basis. National benchmarking indicates

economies of scale. For 2015, LGPS administration costs in England averaged £25 a member, while for London the average was £42 to £49.

Management of IT systems

Managing the IT platform is complex and intensive. The benefits accrue to one scheme only.

Limited access to senior management

The administration of pensions is not integral to any of the Council's priorities and can lack management attention. In addition, responsibility for oversight is shared with the Pensions Committee and Board, with each party not familiar with the monitoring work undertaken elsewhere

- 3.7 We have highlighted a number of challenges from having a small in-house team operating in a challenging and evolving environment. These challenges can be mitigated through having adequate resources both in terms of quantity and quality. Building in resilience requires some excess capacity (again both quality and quantity) at normal times so that ad-hoc issues e.g. staff departures, changes in regulation etc can be handled.
- 3.8 It is relatively rare for in-house team to be 'over' resourced to cope with the unexpected. This is reflected by surveys by the Pensions Regulator that report that small in-house pension teams are less aware of their regulatory duties and less likely to have in place procedures to ensure the completeness and accuracy of data. These findings are consistent with the tone of the LGA report commissioned for Tower Hamlets.
- 3.9 The current structure of the in-house team has seven staff, which is broadly adequate (with no spare capacity) post the completion of the various projects that are ongoing (Payroll data interface and enhancements to deal with auto-enrolment, member self-service and GMP reconciliations). A survey of in-house pension teams for London Boroughs (six responded) indicated team sizes of 4 to 13 with an average of 8.5.

Consideration of Alternative Delivery Options

- 3.10 There are two main alternative means of delivering pension administration services to the Scheme. These are:
 - (a) Co-operation with other Local Authorities
 - (b) Appointing an external third party administrator

Each of these two options is considered below.

Co-operation with Other Local Authorities

- 3.11 Co-operating with other local authorities can be seen as sitting in between an in-house team and fully fledged multi-client third party administrator. The Local Authority groupings have a handful of clients, not many hundreds and focus mostly or entirely on the LGPS. The main advantage they bring is scale of resources. With larger teams there should be less reliance on a single person. Similarly, when handling IT platforms, changing regulations or service enhancing projects the effort is spread across multiple schemes, which should mean lower costs per scheme.
- 3.12 There are three groupings of Local Authorities involving London Boroughs – Orbis (Surrey and East Sussex), Local Pension Partnership (LPFA and Lancashire) and Pensions Shared Service (Wandsworth). In addition the West Yorkshire Pension Fund also offer LGPS administration services, although it has no London Borough's as clients. Brief comments relating to each grouping is attached (appendix 2).
- 3.13 Each of the three London groupings provides pension administration services to four of five London Boroughs. Staff numbers vary between 35 (Pension Shared Service) and 120 (Local Pension Partnership). The parent entities being local authorities have an internal need to provide good quality pension administration (the senior directors will mostly be in the scheme), while for the third party administrators the service is commercially motivated.
- 3.14 Other potential advantages of working with Local Authority groupings include:
- IT economies of scale
 - Bigger grouping can negotiate lower per member IT costs. In addition they are consulted on systems developments and tend to be first adopters of updates.
 - Specialist staff
 - With larger teams, staff can specialise e.g. client facing, IT, regulatory oversight, data quality etc.
 - Standardised client reporting
 - Over time standardised client reporting will have been developed with the input of their various clients.
- 3.15 The London based local authority groupings discussed above can be appointed as a service delegation based on recovery of costs rather than a commercial fee.
- 3.16 In addition to the four existing Local Authority groupings highlighted in appendix 2, there is the possibility of working with other Local Authorities, including councils that face the same challenges as Tower Hamlets. There may even be opportunities for Tower Hamlets to be the host borough.

Setting up a new grouping from scratch will however take longer than joining an existing grouping.

3.17 It would be wrong to suggest that there are no risks with switching from an in-house provider to a local authority grouping. These are the reverse of the advantages of retaining an in-house team e.g.

- Loss of controls and the need to compromise.
- Reliant on third party to report on service standards.
- Key staff being diverted to address new business or other client needs.
- Less direct contact with scheme members and service providers.
- Impact on current in-house staff.

3.18 There are also issues around the transition to the new site and systems. Fortunately all the London based grouping use the same administration system as Tower Hamlets, reducing the transfer complexity.

3.19 Even if most day-to-day administration is transferred externally, some work (employer issues, complaints, contract reporting etc) will remain in-house.

3.20 Retaining continuity of the existing team should be a key goal. Good quality pension staff are increasingly rare and retaining knowledge of Tower Hamlets history is important. Locating the team in the borough or close by will increase the likelihood of continuity.

Appointing an external third party administrator

3.21 The third option identified is appointing a third party administrator by way of a commercial tender. There are many third party administrators who provide pension administration services to private and public sector schemes. Some of the largest pension scheme with 100,000s of scheme members e.g. British Coal Pensions have appointed external third party administrators. Other schemes e.g. Railways, have converted their in-house administrators into commercial entities seeking external business as a way of generating revenue. The key drivers for externalising pension administration are cost reduction and risk management. Pensions is highly specialised; costly if based on manual processes; highly dependent on good technology and requires constant vigilance to identify and comply with the frequent changes in legislation and regulation. Private (and public) sector pension schemes have over the years outsourced most investment management activity to

specialists and see a direct parallel in outsourcing in-house administration to specialist organisations.

3.22 In theory, appointing a third part administrator will magnify both the advantages (cost and resilience) and disadvantages (compromise and loss of control) of local authority groupings.

3.23 Third party administrators can be accessed through the National LGPS Frameworks. This is a relatively new framework (December 2016) and this framework has two lots (full administration services and support services). The providers for lot 1 (full administration services) are:

Capita Employee Benefits
Equiniti
Orbis
West Yorkshire Pension Fund

3.24 A summary of Capita and Equiniti's pension administration scale is included on appendix 2.

3.25 There are many other third party administrators not on the national framework, some of whom may have local authority business. Using the framework has significant procurement benefits. However, a full tender could also be undertaken.

3.26 Local authority experience of third party commercial pension administration has been mixed in recent years. This is often due to the drive to minimise costs, requiring reliance on IT systems to record activity and make calculations with relatively few experienced staff. When IT problems occur, they can have a major impact on scheme members. The other drawback is the use of call centres and on-line portals to interface with scheme members that can make it difficult for a scheme member to resolve a query as for example the 'agent' dealing with the query may have little pensions knowledge. A tender that places a high weighting on service quality, demanding KPI and a low allocation to cost may result in a good quality service.

Conclusion

3.27 The recommendation to review the options available to provide pension administration services reflects a view that although small teams such as Tower Hamlets can offer a more personal service to scheme members they can only do this and maintain robust and compliant processes through good fortune (retaining highly experienced and competent staff) and at a high relative cost.

3.28 Changing the manner in which services are provided aims to provide greater predictability in the service received by scheme members together with an

ability to rigorously monitor the quality of service delivery and increased confidence that the service meets regulatory requirements and has regard for best practice.

- 3.29 Of the two alternatives – multi-authority co-operation and third party outsourcing, the former is preferred as possibly offering the best balance of resilience through scale while not being lost in the crowd. The multi-authority groups are mainly or wholly LGPS focused, their own schemes being LGPS. In addition, their location will aid the retention of existing staff.

Next steps

- 3.30 Should the Committee be content with the proposal to investigate the alternatives above, in-depth reviews of each of the alternatives will be undertaken with proposals made to the next meeting in September.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

- 4.1 The costs of pension administration are paid for from the assets of the pension fund and therefore do not impact directly on the council's General Fund. The paper indicates that the costs associated with changing to a multi-authority provider are unlikely to rise and that the cost per Member of such arrangements are generally lower however, detailed cost estimates have not been sought and will need to be considered before a final decision is reached.

5. LEGAL COMMENTS

- 5.1 The Pensions Committee is required to consider pension matters and ensure that the Council meets its statutory duties in respect of the fund. It is appropriate having regard to these matters for the Committee to receive information from the Pensions Administration team about the performance of the administration function of the pension fund.
- 5.2 Outsourcing Pension functions is likely to have TUPE implications or may result in a redundancy situation depending on the following:
- i) If mobility clauses within the existing employees' contracts do not allow for the employees to work at alternative locations (outside the borough specifically) then the changes to the employees' contracts may be sufficient so as to render those employees potentially redundant and the Council will need to have regard to the consequential cost and/or the loss of skilled employees.
 - ii) The outsourcing of the service to a different provider is likely to mean that staff (subject to point i) above) will transfer pursuant to the TUPE regulations on their existing terms and conditions. Consultation with staff regarding the transfer and implications for their employment will need to take place in good time in advance of the transfer date

5.4 When carrying out its functions as the administering authority of its pension fund, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty).

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The administration costs of running the pension scheme are a very small part of the contributions paid. An efficient administration function will contain costs over the long term, minimising the costs falling on the scheme employers, including the Council.

6.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

7. BEST VALUE (BV) IMPLICATIONS

7.1 In each case decisions to acquire additional services have followed the Council's procurement procedures. All costs are paid for from the assets of the Pension Fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Risks arising from poor administration tend to be reputational but can include additional expenditure through inaccurate benefits, delays in collecting contribution, fines and interest on late payments. The review of the structure of pension administration has a primary aim of minimising the risk of poor administration and to provide the Pensions Committee with assurance that pension risks are being adequately managed.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- Appendix 1 - Current pension administration arrangements for LB
- Appendix 2 - Brief summary of the external administrators

Local Government Act, 1972 Section 100D (As amended)
List of “Background Papers” used in the preparation of this report

- NONE

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Current Arrangements for London Borough Pensions

Barking and Dagenham	in-house
Barnet	Capita
Bexley	LPP
Brent	Capita
Bromley	Liberata UK
Camden	PSS
Croydon	in-house
Ealing	LPP
Enfield	in-house
Greenwich	in-house
Hackney	Equiniti
Hammersmith & Fulham	Orbis
Haringey	in-house
Harrow	in-house
Havering	in-house moving to LPP
Hillingdon	Orbis
Hounslow	Capita
Islington	in-house
Kensington & Chelsea	Orbis
Kingston	London Borough of Sutton
Lambeth	in-house
Lewisham	in-house
Merton	PSS
Newham	LPP
Redbridge	in-house
Richmond	PSS
Southwark	in-house
Sutton	in-house - shared with Kingston
Tower Hamlets	in-house
Waltham Forest	PSS
Wandsworth	PSS
Westminster	Orbis

LGPS based Pension Administration Groups

ORBIS

Orbis is the operating name of Surrey and East Sussex Councils' administration function. Orbis provide administration services to two county scheme (Surrey and East Sussex) and four London Boroughs (Hillingdon, Westminster, Kensington and Chelsea and Hammersmith and Fulham.) These schemes have 250,000 members with Orbis employing 80 staff based in Lewis and Kingston.

Local Pension Partnership

The Local Pension Partnership (LPP) is the name given to the working arrangement between the LPFA and Lancashire Council. The partnership covers all aspects of the two authority's pension funds, in addition pension administration services are provided to a further 13 pension funds comprising two counties, three London Boroughs (Bexley, Ealing and Newham) and 8 Police and Fire Authorities. Bexley and Newham are 2/3rds of OneSource and the other participating Council, Havering, is negotiating with LPP, whose client schemes currently comprise approximately 500,000 scheme members and deal with over 1,000 employers. Currently they have 120 staff based in London, Hertford and Preston. LPP also offer ad-hoc service e.g. governance reviews, project support and interim staffing.

Pension Shared Service

Pensions Shared Service is a grouping of five London Boroughs, being Camden, Merton, Richmond, Waltham Forest and Wandsworth. The five councils have collectively approximately 100,000 scheme members. Currently have approx. 35 staff based at Wandsworth. PSS has indicated that it will not be seeking new clients in the next 18-24 months.

West Yorkshire Pension Fund

Based in the Bradford, West Yorkshire Pension Fund currently administers the LGPS for shared service members over 116,000 active members, total membership number over 368,000 and 630 employers. The majority of the membership work for the main 5 Councils within West Yorkshire. They also administer the Fire Pension Schemes as third party administrators, for 7 Fire and Rescue Authorities. Over the last few years WYPF has expanded its administration business by taking on new Fire clients and the shared service partnership with Lincolnshire Pension Fund. They employ 119 administration staff.

Capita

Capita have provided LGPS administration services for over 40 years having been established in 1974 to administer the Water Authorities. They are now the UK's largest third-party pension's administrator, managing the entitlements of approximately four million individuals, over two million of whom are members of UK Public Sector Schemes. In total, they currently administer seven schemes with over

10,000 active members each and administer the benefits of over 200,000 LGPS Scheme Members for a range of clients including:

- Environment Agency
- London Boroughs of Barnet, Brent, and Hounslow
- West Sussex County Council

Capita also administer the Teachers' Pension Scheme which has almost 1.9 million members and a number of Police Forces. Their pension administration service has approximately 1,300 employees. Their main LGPS team is based in Darlington.

Equiniti

The overall scale of Equiniti's business is not known, however they employ 1,675 staff in pension administration across 13 regional offices. LGPS business is handled from Crawley, although the call centre for first contact is located in Birmingham and is unlikely to have significant LGPS knowledge. The only existing LGPS client mentioned is Hackney and the Crawley LGPS team comprises 11 people. Their public sector business included NHS, Armed Forces, Civil Service and Metropolitan Police.